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C O N F I D E N T I A L TEL AVIV 002123

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E.O. 12958: DECL: 04/08/2014
TAGS: ENRG IS ECONOMY AND FINANCE GOI EXTERNAL LABOR AND COMMERCE
SUBJECT: DETAILS OF EGYPT/ISRAEL GAS PIPELINE APPROVED BY GOVERNMENT

REF: TEL AVIV 1288

Classified By: Economic Counselor Theodore A. Mann for reasons 1.4 (b) and (d).

¶1. (C) Summary. The Egypt/Israel gas pipeline project cleared a crucial hurdle on April 4 when the GOI gave its blessing to the Israel Electric Company (IEC) to negotiate an agreement with the supplier of Egyptian natural gas, Eastern Mediterranean Group (EMG). Under the proposed agreement EMG, a joint Israeli/Egyptian company, will purchase 1.7 billion cubic meters per year of natural gas from Egypt, oversee the construction and operation of a pipeline to Israel, and then sell the gas to IEC. Merhav, EMG's Israeli partner, told Embassy econoff that they expect a final agreement to be signed as early as May, with gas exports beginning in mid-2006. Merhav claims the government decision solved most of the remaining issues on the Israeli side (reftel). End summary.

¶2. (C) On March 7, Embassy econoff spoke with Merhav Senior Vice President Nimrod Novik about the April 4 decision. Novik said that decision taken by the sub-cabinet (comprised of the Ministers of Finance, Infrastructure, and the PM's office) cleared the way for IEC to enter into final negotiations with EMG and the Egyptians. Novik said the government avoided the thorniest issue, which was a demand for each government to issue a guarantee in case either side was unable or unwilling to honor their sides part of the agreement. The GOI decided not to get involved in a mutual guarantee process, but instead will allow the parties (IEC, EMG, Israel Natural Gas Line (INGL), and Egyptian Gas (EGAS)) directly involved to provide the necessary guarantees. For example, Novik said, INGL, the Israeli pipeline builder and operator, will provide a guarantee to IEC in the event that the pipeline in Israel is not ready to receive the gas on time.

¶3. (C) IEC's contract with EMG is for the supply of 1.7 billion cubic meters (BCM). Novik added that the government decision allows IEC to decrease its contracted supply by an amount equivalent to the future amount of gas contracted by any IPP in Israel (see reftel). (Note: Israel has only one natural gas supplier at the current time, the joint Israeli/U.S. consortium Yam Tethys. Prime Minister Sharon decided in 2003 that Egypt, represented by EMG, would be Israel's second supplier. This week, in addition to the decisions regarding Egyptian supply, Israel reportedly settled on British Gas's (BG) offshore Gaza Strip natural gas reserves as Israel's third supplier if there is available demand. According to the press, the sub-cabinet's approval of BG will allow it to negotiate with potential natural gas buyers in Israel. End note.)

¶4. (C) The next step, according to Novik, is a meeting of the IEC Board on April 15 where the board is expected to approve this week's government decision and the parameters of a final agreement to be negotiated with EMG and EGAS beginning the following week in Egypt. Novik expects that Merhav, as part of EMG, and IEC will travel to Egypt on April 20 to begin final negotiations. Novik said he was pleased with this week's events. The project, he asserts, is the most visible link between the two countries and enjoys the support of Prime Minister Sharon and President Mubarak. Novik acknowledged that there are still obstacles to a final agreement, but he is confident that they are diminishing rapidly. Novik asked that Washington consider commending President Mubarak during his upcoming visit to the U.S. for the leadership he has shown in supporting this important bilateral project. And he added that the U.S. should encourage Mubarak "to explore other opportunities for Israeli-Egyptian bilateral cooperation."

¶5. (C) Comment: This week's cabinet decision was a significant step forward for the Egypt/Israel natural gas pipeline, however, the accelerated timetable laid out by Novik is likely to slip. The long history of this project suggests that there could be a few more hurdles to come.

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LeBaron